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No. 08-164

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

VISION SERVICE PLAN,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF OF AMICUS CURIAE NATIONAL TAXPAYERS UNION IN SUPPORT OF PETITIONER

HERBERT F. KOZLOV
REED SMITH LLP
599 Lexington Avenue
New York, NY 10022-7650
(212) 521-5400

RAYMOND A. CARDOZO
Counsel of Record
REED SMITH LLP
Two Embarcadero Center
Suite 2000
San Francisco, CA 94111
(415) 543-8700

Attorneys for Amicus Curiae National Taxpayers Union

218134

COUNSEL PRESS
(800) 274-3321 • (800) 359-6859

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INTEREST OF AMICUS CURIAE[1]

The National Taxpayers Union ("NTU") was founded by concerned taxpayers in 1969. It is a nonprofit, nonpartisan membership organization devoted to protecting the interests of federal, state and local taxpayers though public education, lobbying, and litigation on tax, spending, regulatory and economic issues. NTU represents over 362,000 members in all fifty states.

NTU has long been involved in IRS reform and taxpayer rights issues. For example, the group actively supported the IRS Restructuring and Reform Act of 1998 and in the 10 years since, NTU has pursued additional laws and regulations that will make tax administration simpler, more consistent, and less arbitrary. The petition raises compelling questions regarding a tax exemption that is of crucial importance to many entities that contribute vitally to our society. NTU's goal of obtaining greater predictability, consistency and simplicity in tax administration is very much at stake in this case, and NTU believes its perspective on tax questions will be of assistance to the Court in evaluating the petition.

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1. No counsel for a party authored this brief in whole or in part, and no such counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than the *amicus curiae*, or its members, or counsel, made a monetary contribution to its preparation or submission. The parties have consented to the filing of this brief and have been given the required 10 day notice. Such consents are being lodged herewith.

NTU does not in this brief repeat petitioner's well-reasoned analysis of the Ninth Circuit decision and the problems created thereby. NTU submits this brief solely to highlight three aspects of the Ninth Circuit's opinion that warrant certiorari review. First, by articulating an amorphous test for application of the Internal Revenue Code section 501(c)(4) tax exemption with no guidelines for how to apply the test, the decision creates a quandary for non-profit organizations that depend on the exemption but have no meaningful guidance regarding its application to them. Second, by granting the IRS virtually unlimited discretion to apply an eye-of-the-beholder legal standard, the Ninth Circuit's test fosters undue instability, uncertainty and inconsistency in this area of the law. Third, the courts should leave to the legislative process any decision to depart from the more consistent and predictable interpretation of the exemption that the IRS previously had applied for decades and that Congress had endorsed in its 1986 amendments to the Code.

THE COURT SHOULD GRANT THE PETITION BECAUSE THE QUESTION PRESENTED IS OF EXCEPTIONAL IMPORTANCE, YET THE NINTH CIRCUIT'S DECISION LEAVES THAT IMPORTANT QUESTION UNCERTAIN AND VULNERABLE TO THE WHIM OF THE TAX AGENCY

A. By Employing An Ambiguous Legal Standard To Affirm The IRS's Revocation Of A Tax Exemption That A Non-Profit Organization Had Enjoyed For Over 40 Years, The Ninth Circuit Has Injected Substantial Ambiguity Into A Sector That Needs Certainty

Vision Service Plan ("VSP") is organized and operates in the same way it did nearly a half century ago, when the IRS first recognized its tax exempt status. (Petition at 4, 8) The only appreciable change is that VSP has grown in a manner that makes its healthcare service available to even broader portions of the community. (*Id.*) The language of Internal Revenue Code section 501(c)(4) granting a tax exemption to "social welfare" organizations likewise has not changed at any time since VSP's exemption was recognized in 1960. (*Id.*)

Although there has been no material change in fact or law (other than the 1986 statutory amendments that, as explained in VSP's petition, bolster VSP's position), the IRS has overturned its longstanding interpretation and revoked a tax exemption that VSP had enjoyed for over 40 years. That result not only will cost VSP millions, but it represents an even more disturbing shot across the bow to other non-profit organizations that presently enjoy tax exempt status under Section 501(c)(4).

Prior to the decisions below, many non-profit HMOs could comfortably rely on the Section 501(c)(4) exemption. After all, as VSP details in its petition, the IRS's own Revenue Rulings and internal guidelines, Congress's expressed judgment in the 1986 statutory amendments that added section 501(m) to the Code, and the common law all treated the provision of a valuable public good—healthcare services—to a broad segment of the community—the HMO's subscribers—as generally sufficient to establish the right to an exemption as a social welfare organization. That standard was clear, could be predictably applied, mirrored Congress's expressed intent and appeared settled prior to the decisions below.

The Ninth Circuit's decision, however, endorses a fundamental change in the interpretation and application of Section 501(c)(4). *See, e.g.*, C. Jedrey and C. Buck, *Health Care Organizations*, TAXATION OF EXEMPTS 280 (May/June 2006) at p. 282 ("If the IRS adopted the [district] court's conclusion that operating primarily for the benefit of paying members precludes tax-exempt status for HMOs under Section 501(c)(4)—and one would expect under Section 501(c)(3) as well—the result would be loss of tax exempt status for almost all currently tax-exempt HMOs").

The Ninth Circuit held that a non-profit HMO that provides services to a substantial segment of the community did not qualify as tax-exempt under Section 501(c)(4) because the HMO was not "primarily engaged in promoting the common good and general welfare of the community." (Mem. Disposition at 2) The Ninth Circuit acknowledged that "VSP offers some public

benefits," but held those benefits were "not enough." (*Id.*) The decision views the provision of services to subscribers as an activity that does not benefit the community sufficiently, but did not explain either what additional type of "public benefits" are required to qualify or what quantum of those activities make the grade.

As a result, non-profit HMOs who previously had every reason to believe they were tax exempt, now have a large cause for concern. But since the Ninth Circuit indicated neither the types of activities nor their quantum that will meet its "public benefits" litmus test, these organizations have no way to evaluate the risk that the tax exemption on which they critically depend could be revoked.

As VSP's experience demonstrates, moreover, these non-profit entities also can draw no comfort from the IRS's prior treatment of them as exempt social welfare organizations. If the IRS can abruptly reverse course without any material change in fact or law in the case of an organization that has enjoyed tax exempt status for over 40 years, no other organization can feel safe.

The Ninth Circuit's slender analysis is all the more troubling because, as part of its Internal Revenue Manual, the IRS has published specific audit/examination guidelines to determine whether HMOs and similar entities qualify for exemption under Sections 501(c)(3) or (c)(4).[2] The IRM directs examiners to assess

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2. Internal Revenue Manual 7.8.1, E.O. Examination Guidelines Handbook, Chapter 27, Health Maintenance Organizations (IRM) at http://www.irs.gov/bus_info/tax_pro/irm-part/part07, located at Petitioner's Excerpts of Record (filed below) at 107-108.

whether the organization enrolls more than an "insubstantial" number of persons who are generally unable to obtain affordable health care services or health care insurance. This includes individuals, employer groups consisting of employers having 50 or fewer employees, elderly persons such as persons who qualify for Medicare benefits, low income persons, or others with special health care needs. (IRM § 4.76.31.8.3.2) The IRM also directs examiners to determine whether the HMO's premium calculation methods result in premiums that are "generally affordable." (IRM § 4.76.31.8.3.3) And the examiner should determine whether the HMO is controlled by community interests rather than by health care providers or others who can benefit personally from the HMO's operations; an important factor in this analysis is whether the organization has a substantial conflict of interest policy that minimizes any impermissible private benefit. (IRM § 4.76.31.8.3.4)

Notwithstanding these detailed IRS guidelines addressing the very subject before the Court, the Ninth Circuit did not even mention the guidelines. Although the guidelines are, of course, not controlling,[3] the Ninth Circuit's failure to explain either why VSP failed to fit into those guidelines or why the Court would not apply the guidelines (as the case may be) leaves other HMOs at a loss as to whether they can continue to draw any meaningful predictive value from guidelines that have helped shape their behavior for years. *See* T. Blais, *California Judge Makes Hash of Tax Exempt HMOs in Vision Service Plan*, 7 TAX & FINANCE, Issue 1 (March 2006) at p. 8 ("Historically, the IRS has promoted

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3. *See, e.g., In re Carlson*, 125 F.3d 915, 922 (7th Cir. 1997).

these guidelines informally to HMOs and practitioners, and HMOs have relied upon these standards in developing and monitoring their activities to ensure continued compliance with § 501(c)(4).").

Our law strives for stability and certainty in the law's articulation and enforcement so parties can organize their affairs with predictable legal consequences. That is why courts follow the doctrine of *stare decisis*. "That doctrine permits society to presume that bedrock principles are founded in the law rather than in the proclivities of individuals, and thereby contributes to the integrity of our constitutional system of government, both in appearance and in fact." *Vasquez v. Hillery*, 474 U.S. 254, 265-66 (1986). The doctrine also avoids disturbing settled practices that have emerged in reliance on the earlier precedent. *See, e.g., Rhode Island v. Innis*, 446 U.S. 291, 304 (1980) (Burger, C. J., concurring in judgment) ("The meaning of *Miranda* has become reasonably clear and law enforcement practices have adjusted to its strictures; I would neither overrule *Miranda*, disparage it, nor extend it at this late date").

While "'stare decisis is not an inexorable command,'" *State Oil Co. v. Khan*, 522 U.S. 3, 20 (1997) (*quoting Payne v. Tennessee*, 501 U.S. 808, 828 (1991)), "even in constitutional cases, the doctrine carries such persuasive force that we have always required a departure from precedent to be supported by some 'special justification.'" *United States v. International Business Machines Corp.*, 517 U.S. 843, 856 (1996) (*quoting Payne, supra*, at 842 (Souter, J., concurring) (*in turn quoting Arizona v. Rumsey*, 467 U.S. 203, 212 (1984))). That a legal interpretation has become

embedded in practice is adequate reason not to overrule it—absent an identified justification for doing so. *See Mitchell v. United States*, 526 U.S. 314, 331-332 (1999) (Scalia, J., dissenting) (stating that the fact that a rule has found "'wide acceptance in the legal culture'" is "adequate reason not to overrule" it).

The same concerns that have prompted courts to place a heavy burden of persuasion on those who wish to overturn precedent likewise warrant caution in any departure from an administrative practice that has taken root over four decades. After all, unexplained reversals of long-standing administrative interpretations likewise undermine society's ability to presume "that bedrock principles are founded in the law rather than in the proclivities of individuals." *Vasquez*, 474 U.S. at 265. Caution in departures from established agency practice also promotes society's interests in stability, certainty and predictability in the application of law.

Here, however, the Ninth Circuit and IRS offered little justification for changing course—even though the change is a fundamental one that threatens to upset settled expectations throughout the healthcare sector. That lack of guidance is troubling to those not only in the healthcare sector but far beyond.

Many other organizations who are important to our civic life rely on a Section 501(c)(4) exemption.[4] Given

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4. 501(c)(4) organizations span the political and economic spectrum from the AARP to the Disabled American Veterans to the League of Conservation Voters to the National Rifle Association.

the dearth of well-reasoned precedent articulating the criteria for qualifying as a "social welfare" organization, these organizations also have looked to the IRS's interpretations and guidelines. The Ninth Circuit here, however, issued a 2-page memorandum that simply parroted the language of the statute and the sole regulation adopted under it and offered a conclusory assessment that VSP failed to qualify. The lack of discussion of prior IRS interpretations, guidelines, the statutory scheme as a whole including the 1986 amendments, and pertinent common law leaves other social welfare organizations uncertain as to how much stock they can place in any of these extrinsic aids in construction. The need for this Court's guidance is therefore compelling.

As NTU now explains, moreover, given the many years of administrative experience built into the previously settled interpretation of Section 501(c)(4), the potential implications of an improvident change in that settled practice and Congress's expressed judgment in this area, the Court should hold that the long standing interpretation should govern and the courts should leave any departures from those interpretations to the legislative process.

B. The Legislative Process Is Better Suited To Evaluate The Wisdom Of Any Departure From The View That The Services HMOs Deliver To Their Subscribers Benefit The Community Sufficiently To Support Exemption Under Section 501(c)(4)

Our multi-trillion dollar healthcare system is under intense scrutiny by policymakers, and a growing literature asserts that non-profit HMOs may deliver greater social benefits than for-profit HMOs.[5] But non-profit HMOs who previously could count on a Section 501(c)(4) exemption now face an uncertain future where they lack meaningful guidance on the availability of their exemption and know that the IRS's long-standing recognition of their exemption is no guarantee that the IRS may not abruptly reverse course. Non-profit hospitals and others healthcare organizations that rely on a tax exemption face the same dilemma. These non-profits also can no longer rely on the view that their provision of healthcare to the populations they serve confers sufficient community benefits to support an exemption and must instead guess whether their operations fit within the Ninth Circuit's vague "public benefits" test. Since many of these organizations already

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5. *See, e.g.*, Schlesinger, Mitchell and Gray, *Measuring Community Benefits Provided by Nonprofit and For Profit HMOs*, 40 Inquiry 114 (Summer 2003) (non-profit HMOs are more likely than for-profits to provide subsidies and to support research and other community benefit activities); Tu and Reschovsky, *Assessment of Medical Care by Enrolles in For-Profit and Non-Profit Health Maintenance Organizations*, 346 New England Journal Medicine 1288 (4/25/02) (higher levels of patient satisfaction found in nonprofit HMOs).

face disadvantages in competing with for-profit operators, many may not wait until they suffer VSP's fate and may instead reorganize to operate on a for-profit basis.

Given the potential implications of any such shift, any decision to change the standards by which tax-exemptions in the healthcare field are judged is best left to either Congress or the administrative rule-making process. Doing so permits public comment, thereby allowing for a careful evaluation of the realities of the marketplace, the experience of the last four decades and all other relevant considerations.

Neither the Ninth Circuit, the district court nor the IRS even purported to perform the type of comprehensive evaluation that is warranted for a change of this magnitude. Since they did not do so, it would have been more prudent to stick with the interpretation that previously had prevailed for over 40 years. That interpretation had the benefit of many years of practical application, and Congress endorsed that interpretation in its 1986 statutory amendments.

The above concerns extend well beyond healthcare non-profits. The availability of a tax exemption may prove to be the difference between survival or demise for many of these organizations. These entities and the persons they serve are entitled to better guidance. They should not be forced to proceed under a regime where an undefined, eye-of-the-beholder "public benefit" standard is left to the whim of an agency that has demonstrated it may disturb settled expectations without advancing any compelling justification for

changing course. Our society's interest in greater predictability, consistency and simplicity in tax administration is yet another reason why this case is worthy of this Court's consideration.

CONCLUSION

The petition for writ of certiorari should be granted.

Respectfully submitted,

HERBERT F. KOZLOV
REED SMITH LLP
599 Lexington Avenue
New York, NY 10022-7650
(212) 521-5400

RAYMOND A. CARDOZO
Counsel of Record
REED SMITH LLP
Two Embarcadero Center
Suite 2000
San Francisco, CA 94111
(415) 543-8700

Attorneys for Amicus Curiae
National Taxpayers Union